IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 67 of 1997
with
INCOME TAX REFERENCE Nos.32, 36, 37, 38, 39, 40, 43, 44,
45, 46, 47, 74, 75, 76, 77, 78, 79, 80,
81, 82, 83 and 88 1997
(Twenty three matters)

For Approval and Signature:

HON'BLE MR.JUSTICE M.S.SHAH
and
HON'BLE MR.JUSTICE A.M.KAPADIA

==========

1. Whether Reporters of Local Papers may be allowed to see the judgements? : NO

2. To be referred to the Reporter or not? : NO

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the concerned Magistrate/Magistrates,Judge/Judges,Tribunal/Tribunals? : NO

COMMISSIONER OF INCOME TAX

Versus

SINIVALI TRUST

Appearance:

In ITR Nos. 67, 74 to 83 & 88 of 1997
MR MANISH R BHATT for Petitioner No. 1
SERVED BY RPAD - (N) for Respondent No. 1

In ITR Nos. 40, 43 and 44 of 1997
MR BHARAT NAIK for Petitioner No. 1
SERVED BY RPAD - (N) for Respondent No. 1

In ITR Nos. 32, 36, 37, 38 & 39 of 1997
MRS MAUNA M BHATT for Petitioner No. 1

SERVED BY RPAD - (N) for Respondent No. 1

In ITR Nos. 45, 46 & 47 of 1997
MR TANVISH U BHATT for Petitioner No. 1
SERVED BY RPAD - (N) for Respondent No. 1

CORAM : HON'BLE MR.JUSTICE M.S.SHAH
and
HON'BLE MR.JUSTICE A.M.KAPADIA
Date of decision: 11/02/2004

COMMON ORAL JUDGEMENT

(Per : HON'BLE MR.JUSTICE M.S.SHAH)

In these references at the instance of the revenue under Section 256(1) of the Income-tax Act, 1961 (hereinafter referred to as "the Act"), the following questions have been referred for our opinion for assessment years 1984-85 and 1985-86 :-

1. Whether the Appellate Tribunal is right in law and on facts in directing the Assessing Officer to charge the tax at normal rate instead of maximum marginal rate ?

2. Whether the Appellate Tribunal is right in law and on facts in deleting the interest charged u/s.217 of the Act ?

2. We have heard learned counsel for the revenue Mr Manish R Bhatt in ITR Nos. 67, 74 to 83 & 88 of 1997, Mr Bharat Naik in ITR Nos. 40, 43 and 44 of 1997, Mrs Mauna Bhatt in in ITR Nos. 32, 36, 37, 38 & 39 of 1997 and Mr Tanvish U Bhatt in ITR Nos. 45, 46 & 47 of 1997. Though served, none appears for the respondent-assessees.

3. The facts found and the findings given by the Tribunal as set out in the common order of the Tribunal giving rise to these references are as under :-

3.1 One Mr Ashokkumar S Vaswani settled Rs.5,000/and formed Sharda Trust as per the trust deed on 28.1.1983 with the three trustees. As per the trust deed, there were 20 beneficiaries each having 5% beneficial interest in the main trust. Sharda Trust carried on business during the accounting year relevant to the assessment year 1984-85 and from the business so carried on Sharda Trust earned profit of Rs.3,20,000/-. The income so

earned was declared in the assessment year 1984-85 and the same was assessed in the hands of Sharda Trust under Section 143(3). As the trust was specific and the shares of beneficiaries were determinate, no tax was levied in the case of Sharda Trust. The income determined was, however, allocated amongst the beneficiaries at the rate of 5% thereof, which came to Rs.16,000/- in each case.

3.2 Taking the case of RD Trust as an illustrative case, the Tribunal found that RD Trust is one of the beneficiaries of Sharda Trust. As per its trust deed, there are two beneficiaries - Miss Rita and Mrs Devi and as per the claim of the assessee, none of these two beneficiaries are further beneficiary in any other trust and none of them have income exceeding the maximum limit not liable to tax. The assessee has thus claimed that as per the proviso to Section 164(1) the income declared in the hands of RD Trust is liable to be taxed at normal rate. According to the revenue, these trusts have been created as a device to reduce or avoid the tax payable and the ratio of the decision of the Hon'ble Supreme Court in the case of McDowell & Co. is applicable to the facts of the case.

3.3 The Tribunal found that the revenue has accepted Sharda Trust (main trust) as genuine while completing its assessment. The assessment so made has not been disturbed by taking remedial action. There is rather no finding given by the Assessing Officer that formation of Sharda Trust is a part of the device to avoid payment of legitimate taxes. The Assessing Officer has treated it as a specific trust and the income earned by it has been allocated amongst the beneficiaries as per their share ratio specified in the trust deed. This shows that the revenue saw no colurable device so far as the formation of Sharda Trust is concerned.

3.4 The Tribunal further found that in the case of the assessees who are beneficiaries of Sharda Trust (the beneficiary assessees themselves happen to be trusts), none of the individual beneficiaries of the beneficiary trusts is a beneficiary in any other trust and none of the beneficiary trusts or the individual beneficiaries in such beneficiary trusts had income exceeding the maximum amount not liable to tax. The Tribunal held that the view taken by the Commissioner of Income-tax (Appeals) that the beneficiary trusts were liable to be charged at normal rate as per the proviso to Section 164(1) of the Act was the correct view and that the substantive part of Section 164(1) did not apply to the facts of the case. The Tribunal also found that the assessment on the

beneficiary trusts was made on protective basis without prejudice to the decision that may be taken in the case of the main trust. In the case of main trust, the income declared has not been taxed. The assessment on the income of the beneficiaries has not been made in substantive capacity in the hands of any other entity. The income is treated to have been taxed substantively in the case of the assessee-trust.

3.5 The Tribunal, therefore, held that there was no evidence to show that the beneficiary trusts were formed as a device to avoid tax so as to fall within the ambit of the ratio of the Supreme Court in the case of McDowell & Co..

3.6 Since the Tribunal did not find any infirmity with the decision of the Commissioner of Income-tax (Appeals) on merits, the question of charging interest under Section 217 of the Act did not survive.

4. The learned counsel for the revenue have submitted that the case was covered by the substantive part of Section 164(1) of the Act and, therefore, maximum marginal rate was applicable. The learned counsel also submitted that the entire thing was a colourable device so as to avoid tax liability and, therefore, both the Commissioner of Income-tax (Appeals) and the Tribunal erred in setting aside the protective assessment made by the Assessing Officer against the beneficiary trust.

5. At the outset, we would like to make it clear that though the revenue had proposed three questions for reference to this Court under Section 256(1) of the Act, the Tribunal referred only question Nos. 1 and 3 which are set out hereinabove. Question No.2 which was proposed by the revenue, but was not referred by the Tribunal, was as under :-

> "2. Whether the Appellate Tribunal is right in law and on facts in not appreciating that the assessee's case is of a conduit pipe of trust wherein the ultimate beneficiaries are other than beneficiary mentioned in the settlement deed ?"

The Tribunal declined to refer to the said question on the ground that the finding by which the Tribunal rejected the revenue's contention that the trusts were formed as a colourable device was based on proper appreciating of facts and material on record. It

appears that the revenue did not take any steps to have the said proposed question No.2 referred to this Court under Section 256(2) of the Act. In this view of the matter, we have not permitted the learned counsel for the revenue to raise any contention based on the plea that the arrangement was a colourable device to avoid tax liability.

6. Apart from the above aspect, we have also noted the finding given by the Tribunal that the Assessing Officer found formation of the main trust i.e. Sharda Trust as a genuine one and since the assessment of Sharda Trust has not been disturbed in any manner and since the income of the Sharda Trust was allocated amongst the 20 beneficiaries with determinate share at 5% each i.e. at Rs.16,000/- each for assessment year 1984-85 and since each of the beneficiary trusts allocated its income to its beneficiaries with determinate shares and each of those beneficiaries was not beneficiary in any other trust and the income of such individual beneficiary did not exceed the exemption limit, the proviso to Section 164(1) was applicable and not the substantive part of Section 164(1). The substantive part of Section 164(1) would apply where the individual shares of the beneficiaries are indeterminate or not known and the proviso is not attracted. In the facts of the instant case, the findings given by the Tribunal are that the shares of the beneficiaries of Sharda Trust were determinate at 5% for each beneficiary and that the individual beneficiaries of those beneficiary trust were covered by proviso (i) to Section 164(1) in as much as none of the beneficiaries had other income chargeable under the Income-tax Act exceeding the maximum amount not chargeable to tax and none of the individual beneficiaries is a beneficiary under any other trust. In view of the aforesaid clear findings given by the Tribunal, we are of the view that the Tribunal was right in directing the Assessing Officer to charge the tax as normal rate instead of maximum marginal rate.

7. We accordingly answer question No.1 in the affirmative i.e. in favour of the assessee and against the revenue.

8. Coming to the next question about interest under Section 217 of the Act, since the same is a consequential question and since the Tribunal held in favour of the assessee and we have also answered question No.1 in the affirmative, the question of interest under Section 217 does not survive and, therefore, the Tribunal rightly directed deletion of interest under section 217 of the

Act.

9. We accordingly answer question No.2 referred by the Tribunal in the affirmative i.e. in favour of the assessee and against the revenue.

10. All these references accordingly stand disposed of.

(M.S. Shah, J.)

(A.M. Kapadia, J.)

sundar/-